UNITED STATES DISTRICT COURT
FOR THE DISTRICT OF RHODE ISLAND

ALBERT A. GRAY, ADMINISTRATOR, ET AL.	:	
Plaintiffs	:	
v.	:	Civil Action No. 04-312L
JEFFREY DERDERIAN, ET AL.	:	
Defendants	:	

MOTION OF PROPERTY AND CASUALTY INSURANCE ASSOCIATION OF AMERICA FOR LEAVE TO FILE AMICUS CURIAE BRIEF

Property and Casualty Insurance Association of America ("PCI") respectfully moves for leave to file the accompanying amicus curiae brief in support of Defendant, Essex Insurance Company's ("Essex") motion to dismiss the plaintiffs' complaint against Essex. PCI should be granted leave to file the amicus brief because PCI and its members interests are at the epicenter of this case. PCI's views and perspective will assist the Court in its review of the issues before it. PCI's views and perspective will also assist the Court in gauging the impact an adverse ruling will have on the insurance industry as a whole if the plaintiff's allegations are not rejected. The plaintiffs' complaint alleges that Essex negligently conducted an inspection in connection with the issuance of a general commercial insurance policy to the owners of the premises where the Station Nightclub fire occurred. The issue before this Court is whether the plaintiffs' complaint states a cause of action recognized by the state of Rhode Island.

PCI is a trade group representing more than 1,000 property and casualty insurance companies. PCI members are domiciled in, and transact business in, all 50 states, plus the District of Columbia and Puerto Rico. Its member companies account for $171 billion in direct

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written premiums. They account for 48.2% of all personal auto premiums written in the United States, and 37% of all homeowners' premiums, with personal line writers of commercial and miscellaneous property/casualty lines. In addition to the diversified product lines they write, PCI members include all types of insurance companies, including stocks, mutuals, and companies that write on a non-admitted basis. The PCI membership is literally a cross-section of the U.S. property and casualty insurance industry. In 2002, PCI members accounted for 68.0% of the homeowners' insurance premiums in Rhode Island, 70.4% of the personal automobile insurance policies issued in Rhode Island and wrote $772,200,000 of direct written premiums in Rhode Island. Thirteen PCI members are domiciled in Rhode Island. PCI is the nation's premier non-profit insurer trade association, representing over 1,000 companies that write 39.1 percent of the nation's automobile, homeowners, business, and workers compensation insurance. PCI is an advocate for sound public policy that fosters a healthy and competitive insurance marketplace. The association serves as the voice of the property/casualty insurance industry before state and federal policymakers; state and federal courts; key insurance industry, governmental, and business groups; the news media; and the public.

PCI and its member insurance carriers have a direct interest in this case because it involves a potential expansion of Rhode Island liability law concerning all insurance companies, and the interpretation and application of the state statute dealing with an insurer's inspection immunity. PCI explains in its proposed amicus brief why the plaintiffs' allegations can not stand. The proposed brief reviews the text of the inspection immunity statute, and the context in which it should be read and interpreted by the Court. The proposed brief also explains why the plaintiffs' theory of liability against Essex, if not rejected, threatens great harm to the insurance industry. PCI has a special perspective because it is familiar with the manner in which

inspection immunity statutes operate around the country in the insurance industry. The Court should allow PCI's voice to be heard in this case, which vitally affects PCI's interests.

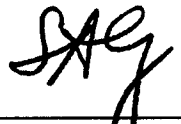
"Federal courts have discretion to permit participation of amici where such participation will not prejudice any party and may be of assistance to the court." *Strougo v. Scudder, Stevens & Clark, Inc.*, 1997 WL 473566 (S.D.N.Y. Aug. 18, 1997) (citing *Vulcan Society of New York City Fire Dep't, Inc. v. Civil Service Comm'n*, 490 F.2d 387, 391 (2d Cir. 1973)). See also *Zell/Merrill Lynch Real Estate Opportunity Partners Limited Partnership III v. Rockefeller Center Properties, Inc.*, 1996 WL 120672 (S.D.N.Y. March 19, 1996) (granting amicus leave to appear and argue, citing cases "uniform in support of a district court's broad discretion to permit or deny amici appearances"); *United States v. Gotti*, 755 F. Supp. 1157, 1158 (E.D.N.Y. 1991) (amici can "provide supplementary assistance to existing counsel and insur[e] a complete and plenary presentation of difficult issues so that the court may reach a proper decision").

For the foregoing reasons, the Court should grant leave to PCI to file the accompanying amicus curiae brief.

Respectfully submitted,

PROPERTY AND CASUALTY INSURANCE ASSOCIATION OF AMERICA
By its Attorneys,

HOLLAND & KNIGHT LLP



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CERTIFICATION

I certify that on 16th day of November, 2004, I served a true copy of the within document via first class mail, postage prepaid to the parties listed below.

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UNITED STATES DISTRICT COURT
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Plaintiffs

v.

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Defendants

C.A. No.: 04-312L

BRIEF OF AMICUS CURIAE, PROPERTY AND CASUALTY INSURANCE ASSOCIATION OF AMERICA, IN SUPPORT OF DEFENDANT, ESSEX INSURANCE COMPANY'S MOTION TO DISMISS

INTRODUCTION

In this brief Property and Casualty Insurance Association of America focuses on and addresses two issues:

1. Whether Essex Insurance Company is immune from liability by virtue of R.I. Gen. Laws §27-8-15.

2. Whether public policy dictates that this Court expand Rhode Island law to recognize a tort of negligent insurance inspection.

This action arises out of The Station nightclub fire. Rhode Island General Laws § 27-8-15, enacted in 1988, immunizes insurance companies from claims relating to inspections conducted in connection with the issuance of insurance policies, including casualty policies. A general liability insurance policy is a specie of casualty insurance policy. Essex Insurance Company issued a policy of general liability insurance to the owners of The Station nightclub. Essex did not create the condition that was the proximate cause of the personal injuries, death

and loss described in the Plaintiffs' complaint. The Court should dismiss the Plaintiffs' complaint as to Essex Insurance Company.

Further, it would be a great leap for this Court to rule that a cause of action exists in Rhode Island for the alleged tort of negligent insurance inspection. First, Rhode Island as a matter of law and policy has determined that so-called negligent insurance inspections will not lead to the imposition of liability on insurance carriers. Second, the Supreme Court of Rhode Island has not ventured to extend such liability to insurance carriers, and under the prior rulings regarding Restatement (Second) of Torts § 342A, probably never will.

FACTUAL BACKGROUND

The tragic facts leading up to the filing of the Plaintiffs' complaint are well known to the Court. The Station nightclub caught fire on February 20, 2003, killing 100 people and injuring more than 200. The fire started when pyrotechnics set off by Great White, the rock band playing that night, ignited flammable soundproofing foam behind the stage.

The Plaintiffs' complaint contains generalized allegations that Essex negligently conducted an inspection of The Station nightclub in connection with the issuance of a policy of liability insurance to the owners of The Station. Essex has filed a motion to dismiss the Plaintiffs' claims against Essex.

ARGUMENT

I. Rhode Island General Laws §27-8-15 Provides Essex Immunity From Liability for the Plaintiffs' Alleged Cause of Action Against Essex

A. A policy of "casualty insurance" as used in §27-8-15 includes a liability insurance policy.

Rhode Island General Laws § 27-8-15 (the "Inspection Statute") provides as follows:

> The furnishing of, or failure to furnish, insurance inspections or advisory services in connection with or incidental to the issuance or renewal of a policy of

> property, casualty or boiler and machinery insurance shall not subject the insurer, whether domestic or foreign, its agents, employees, or service contractors, to liability for damages from injury, death, or loss occurring as a result of any act or omission in the course of those services. This section shall not apply in the event the active negligence of the insurer, its agent, employee or service contractor, created the condition that was the proximate cause of injury, death or loss.

R.I. Gen. Laws § 27-8-15.

The Inspection Statute refers to the " ... issuance or renewal of a policy of ... casualty ... insurance ..." *Id.* The term "casualty insurance" is not defined in the Inspection Statute or in the title dealing with insurance. *Cf.* Del. Code Ann. tit. 18, § 906 (defining "casualty insurance" in the broadest possible terms to include, *inter alia*, vehicle insurance, liability insurance, workers' compensation, burglary and theft insurance, boiler and machinery insurance, medical negligence insurance, livestock insurance, and insurance against any other kind of loss, damage or liability properly a subject of insurance that is not within any other kind of insurance defined under law); Mich. Comp. Laws § 500.624 (providing similarly broad definition of casualty insurance). Fundamental principles of statutory construction, however, dictate that terms, unless otherwise defined, carry their ordinary meaning. This Court, therefore, must apply the plain, ordinary and generally accepted meaning of the words set forth in the statute. *See, e.g., Champlin's Realty Associates, L.P. v. Tillson*, 823 A.2d 1162, 1165 (R.I. 2003); *Pier House Inn, Inc. v. 421 Corp.*, 812 A.2d 799, 804 (R.I. 2002); *State v. Bryant*, 670 A.2d 776 (R.I. 1996); *Rhode Island Chamber of Commerce v. Hackett*, 122 R.I. 686, 690, 411 A.2d 300, 303 (1980). This Court has ample reliable authority upon which to rely to determine the meaning of "casualty insurance" as used in the Inspection Statute.

The term "casualty insurance" has a generally accepted and well defined meaning. "As a general rule 'casualty insurance' covers accidental injury both to persons and to property and has, in fact, been defined as insurance against loss through accidents or casualties resulting in bodily

injury or death. The term is also used to embrace coverages under various liability policies."

Couch on Insurance, Third Edition, §1:28 Casualty Insurance.

Another authority describes "casualty insurance" in the following manner.

> The subject of casualty insurance deals with one of the most vital fields of insurance law today, one which concerns nearly every person in the country, and which is rapidly expanding. The high frequency of automobile accidents, and the enormous number of persons killed or injured annually brings automobile insurance companies constantly to the fore in investigating claims, defending lawsuits arising therefrom, and paying judgments recovered by or on behalf of such persons. The rights and duties of those companies have brought into being a vast body of insurance law which two decades ago was almost unknown. Compensation acts, compensation policies, with the companion coverage of liability at common law to employees, and employer's liability insurance, have great significance to every employer of labor and every employee. Public liability insurance upon buildings, elevators, beauty shops, dram shops, and hospitals, when coupled with more personal liability fields such as malpractice insurance, contractor's liability, products liability, and insurance protecting against liability in almost every phase of business or recreational activity, have rendered this subject one of intimate concern to lawyers and laymen alike. It is apparent that different matters of construction may arise in each of these diverse fields – yet they all go back to the fundamental question of the liability of the named insured to the person injured, and to the further question of whether the policy in question covered the particular activity which produced the injury.

Appleman on Insurance Law, 2003 Cumulative Supplement, Volume 6B, § 4251 Introductory.

The preeminent insurance law textbook defines "casualty insurance" as follows.

> Under the combined influence of voluntary specialization and statutory classification for regulation, insurance contracts and organizations in the United States have developed into three main classes based on the nature of the risk covered. These classes are commonly referred to as life, fire and marine, and casualty insurance.
>
> A still broader combination of underwriting includes life insurance as well as casualty and fire and marine, and is known as "all-line" underwriting. At present some fleets do such all-line underwriting.
>
> Despite multiple-line and all-line developments, the threefold classification of types of insurance is still important. Multiple-line legislation has not abolished the classes of insurance but has merely authorized one insurer to operate in the entire field of insurance other than life. Many companies still limit themselves for business and legal reasons to only a small part of the field that they might occupy. Also distinctive regulations, doctrines, and practices with respect to ties of transportation and communication; and personal property floater risks.

Basic Text on Insurance Law by Robert K. Keeton, Section 1.3, Classification by the Nature of the Risks, § 1.3(a), Generally.

Professor Keeton further describes casualty insurance by including the sub-parts of casualty insurance lines. "Casualty insurance includes liability, workmen's compensation, accident and health, glass, burglary and theft, boiler and machinery, property damage, collision, and credit insurance and fidelity and surety bonds." Id., § 1.3(d), Casualty Insurance. *Accord* Del. Code Ann. tit. 18, § 906; Mich. Comp. Laws § 500.624.

Another definition of "casualty insurance" is this one. "Casualty Insurance. An agreement to indemnify against any loss resulting from a broad group of causes such as legal liability, theft, accident, property damage, and workers' compensation. The meaning of casualty insurance has become blurred because of the rapid increase in different types of insurance coverage. Cf. accident insurance." *Black's Law Dictionary*, Seventh Edition, p. 803.

A further definition of "casualty insurance" is this one:

> Casualty insurance traditionally refers to many different lines or coverages other than life or health, including automobile and general liability; employers' liability; plate glass insurance; professional liability; errors and omissions insurance; burglary, robbery and forgery insurance; aviation insurance; and workers' compensation insurance. Boiler and machinery insurance was historically included but is increasingly classified as property insurance. A typical characteristic of casualty insurance is indemnity for bodily injury or property damage to third parties caused by negligent acts or omissions of the insured.

Rupp's Insurance & Risk Management Glossary, 2002, NILS Publishing.

Rhode Island General Laws § 27-2.4-9 alludes to the breadth of the term "casualty insurance." This statute provides that an insurance producer (meaning a broker or agent) "may receive qualification for a license in one or more of the following lines of authority:

. . . .

(4) Casualty insurance coverage against legal liability, including that for death, injury or disability or damage to real or personal property."

R.I. Gen. Laws § 27-2.4-9(a).

As described above, casualty insurance is a broad category of insurance. Liability insurance policies, such as the one issued by Essex to the owners of The Station nightclub, is a sub-category within the definition of casualty insurance. In their memorandum, the Plaintiffs rely on statutory headings to argue that liability insurance is a separate specie of insurance. The Plaintiffs reliance is misplaced. The fact that the Rhode Island General Assembly chose to pass specific statutes dealing with details of certain sub-categories of insurance coverages (e.g., fire insurance in chapter 27-5, fire and marine in chapter 27-6, workers compensation in chapter 27-7.1) does not alter the basic definition of casualty insurance. The relationship between insurance and casualty insurance and liability insurance is analogous to the categories of the Linnaean classification system. The Linnaean taxonomy is a formal system for classifying and naming living things based on a simple hierarchical structure, from most general to most similar. Each item is classified in a series of categories from the most inclusive (Kingdom) down to the most individualized (Species). Insurance, therefore, is the most general category of classification, followed by the more specific category of casualty insurance, and finally the most specific, liability insurance.

B. Essex issued a policy of casualty insurance to the owners of The Station nightclub.

Essex issued a policy of casualty insurance to the owners of The Station nightclub, specifically a commercial general liability policy. One of the key concepts of liability coverage is that it is comprehensive in nature. This means the policy (insuring agreement) covers all hazards within the scope of the insuring agreement that are not otherwise excluded. It is likewise

comprehensive in that it provides automatic coverage for new locations and activities of a business, which come about after policy inception and throughout the policy term. Commercial General Liability (CGL) is the standard commercial liability policy used to insure businesses. There are three primary coverage sections that make up a CGL policy: premises liability, products liability, and completed operations. Premises liability covers liability for accidental injury, including death, or property damage that results from either a condition on the business premises or on business operations in progress, whether on or away from the premises. A products liability hazard exists for any business that manufactures, sells, handles, or distributes goods or products. The hazard is the potential liability for bodily injury or property damage that arises out of the business's goods or products. Completed operations covers potential liability for bodily injury or property damage that arises out of the business's completed work.

The policy that Essex issued to the owners of The Station nightclub was a CGL policy. As discussed above, general liability insurance policies are a type or sub-category of casualty insurance as referred to in R.I. Gen Laws § 27-8-15. Because the policy comes within the purview of the statute, as a matter of law Essex is not subject to liability for the losses claimed by plaintiffs.

C. Essex did not engage in active negligence to create the condition that was the proximate cause of the injury death or loss.

Rhode Island General Laws § 27-8-15 renders the immunity for lawsuits invalid "... in the event the active negligence of the insurer, its agent, employee or service contractor, created the condition that was the proximate cause of injury, death or loss." R.I. Gen. Laws § 27-8-15 (emphasis added). The term "active negligence" is not defined in the statute and the Rhode Island Supreme Court has not had occasion to consider what constitutes "active negligence" within the meaning of § 27-8-15. Where the General Assembly has not defined a statutory term,

it will be given its plain, ordinary and generally accepted meaning. *See, e.g., Champlin's Realty Associates, L.P.*, 823 A.2d at 1165. Opinions of the Rhode Island Supreme Court provide clear guidance on what type of conduct constituted active negligence, as distinguished from passive negligence.

In *Perry v. St. Jean*, 100 R.I. 622, 218 A.2d 484 (1966), in the context of premises liability, the Court explained:

> [P]assive negligence' denotes negligence which permits defects, obstacles or pitfalls to exist upon the premises, in other words, negligence which causes dangers arising from the physical condition of the land itself. 'Active negligence', on the other hand, is negligence occurring in connection with activities conducted on the premises, as, for example, negligence in the operation of machinery or of moving vehicles whereby a person lawfully upon the premises is injured.

100 R.I. at 624 (quotations and citation omitted).

In *Hone v. Lakeside Swimming Pool & Supply Co.*, 114 R.I. 394, 398, 333 A.2d 430 (1975), the Court held that a defendant's conduct in failing to cover or surround with barriers an excavation, into which a child fell and sustained injuries, did "not come within the definition of active negligence as set forth in *Perry* v. *St. Jean."*

In *Greco v. Farago*, 477 A.2d 98 (R.I. 1984), the Court held that corporate officers and supervisors of an injured employee who allegedly failed to provide a safe place of employment could not be held liable in tort as fellow employees, due to the immunity afforded by the Workers' Compensation Act, because they had not engaged in conduct constituting "active negligence."

These Rhode Island cases make clear that "active negligence" encompasses only affirmative negligent conduct; situations where "the defendant was actually doing something at the time of the injury." *Mailloux v. Steve Soucy Const. Co., Inc.* 116 R.I. 348, 353, 356 A.2d 493 (R.I. 1976). This well-established meaning of the term "active negligence," as derived from the

common law, should also be applied to R.I. Gen. Laws § 27-8-15. *See Rhode Island Student Loan Authority v. NELS, Inc.*, 550 A.2d 624, 629 (R.I. 1988) ("In enacting a statute, the Legislature is presumed to know the state of existing relevant law, including the common law affecting a subject on which legislators undertake to legislate.") (citations omitted); *Knowles v. Ponton*, 96 R.I. 156, 190 A.2d 4 (1963) (explaining that legislative enactments will be construed to alter the common law only where the General Assembly has made that purpose clear).

Under the foregoing case law, it is manifest that negligently allowing a dangerous condition to exist does not constitute "active negligence" within the common meaning of the term. Cases from other jurisdictions addressing the issue in the context of claims against insurers buttress this conclusion.

In *Samuels Recycling Co. v. CNA Ins. Companies*, 588 N.W.2d 385 (Wis. Ct. App. 1998), Samuels contended that CNA failed to provide, or negligently provided, loss control services. Samuels offered evidence of the following in support of this claim: CNA did not train its loss control representatives to inspect for pollution; CNA instructed Samuels to water its battery breaking area and operations without warning them that the contaminated water should be collected and treated; and, after discussion with Samuels about an oil leak, CNA failed to make a recommendation or express any disagreement with Samuels' inadequate remedy of digging a trench to catch future leakage. The trial and appellate courts concluded that the "active negligence" exception did not apply. Samuels contended that CNA's "active negligence" led to Samuels watering its battery breaking area and digging a trench to catch an oil leak. However, there is no evidence that the alleged negligence "created the condition that was the proximate cause" of the loss, as required by Wisconsin Statutes § 895.44, the state's insurance inspection statute.

Hamel v. Factory Mutual Engineering Assoc., 409 Mass. 33, 564 N.E.2d 395 (1990), was an action arising from an industrial accident in which the plaintiff claimed that the defendant insurers' negligence in inspecting the factory where her husband worked, and in making safety recommendations, proximately caused her husband's death. The Massachusetts Supreme Judicial Court ruled that there was no error in allowing the defendant's motion for summary judgment, on the ground that the insurer was protected from liability under G.L. ch. 143, § 16A, the Massachusetts inspection statute. The safety recommendations made by the defendant, while apparently not adequate to prevent the accident, did not increase any risk that already existed at the factory. The Court noted the "Legislature intended to exempt insurers from liability for safety inspections and for making recommendations to promote safety unless the insurer by its actions increases the safety risk at the facility inspected." *Hamel*, 409 Mass. at 37.

The court in *Mier v. Staley*, 329 N.E.2d 1 (Ill. App. 3d 1975), held that a manufacturer's general liability insurer was immune from a suit brought by an employee of the manufacturer who alleged she was injured as a result of the insurer's negligence in inspecting the manufacturer's property. The evidence indicated an employee of a manufacturer was injured when she fell off a man lift in the employer's factory. She subsequently commenced an action against the employer's general liability insurer, alleging her injuries were caused, in part, by the insurer's negligence in performing safety inspections of the employer's factory. The appellate court affirmed the trial court's dismissal of the action, stating that Ill. Rev. Stat. ch. 48 § 138.5(a) (1969), a statute which granted immunity to an insurer in suits based on the negligent performance of safety inspections, was applicable to the employer's general liability insurer, as the language of the statute did not limit immunity to the workers' compensation insurer. In reviewing the constitutionality of the provision, the court noted the legislature's apparent

purpose was to promote industrial safety inspections and that the legislature had the power to promote safety by whatever means were reasonable. The court also stated the classification of general liability insurers with other persons immune was not arbitrary or unreasonable and that the reasons which applied to the granting of immunity to workers' compensation insurers also applied to liability insurers.

In *A. O. Smith Corp. v. Viking Corp.* 79 F.R.D. 91 (E.D. Wis. 1978) (applying Wisconsin law), the court recognized that an insurer which was actively negligent was not entitled to the immunity offered an inspector under Wisconsin Statutes § 895.44, but stated, in granting summary judgment to an insurance company allegedly negligent in performing its inspections of a sprinkler system that apparently failed during a fire, that the statute applied because there was no allegation and no contention that the inspections or advice provided by the insurer, whether proper or improper, created the condition which caused the fire.

The court in *Burns v. State Compensation Ins. Fund* , 71 Cal. Rptr. 326 (Cal. Ct. App. 1968), held that an insurance bureau enjoyed immunity from civil suits for any negligence issuing from its inspection of an employer's plants, since such inspections were actions taken pursuant to the authority conferred on the bureau by statute. The record indicated that an employee of a saw mill who sustained serious injuries commenced an action for damages against the inspection rating bureau, an unincorporated association comprised solely of workers' compensation insurers licensed to do business in the state. The bureau's motion for summary judgment was granted and the appellate court affirmed, stating that under California Insurance Code, Division 2, Part 3, Article 3 (§§ 11750-11759), an insurance rating organization such as the bureau was afforded immunity. In so holding, the court noted the statute expressly authorized such rating organizations to make inspections of places of employment and stated that

Cal. Insurance Code § 11758 provided that no action taken pursuant to the authority conferred by the article would constitute a violation of or grounds for civil proceedings under any other state law. It concluded that the bureau enjoyed immunity from civil suits for any negligence arising out of inspection of employment plants since the inspections were taken pursuant to the authority conferred by statute. The court also noted that Cal. Insurance Code § 11759, added Stats. 1967, ch. 1083 § 1, a statute which exempted organizations such as the insurance bureau from liability for inspection deficiencies but which became effective subsequent to the present action, supported its interpretation of the statutes because the statute provided it was not to be construed as implying a legislative recognition that a liability had existed or would exist except for the enactment of the statute.

Both Rhode Island case law defining the term "active negligence," and case law from other jurisdictions instruct there was no active negligence on the part of Essex that created the condition that was the proximate cause of cause of injury, death or loss in The Station nightclub fire. Essex did not install the soundproofing foam insulation on the walls of the nightclub. It did not build the exit doors. It did not place exit signs in the nightclub. It was not involved in the pyrotechnic display that ignited the fire. It merely issued a GCL policy, a specie of casualty insurance, to the owners of The Station, and is alleged to have conducted a negligent inspection of the premises thereby allowing a dangerous condition to exist. This is precisely the type of passive negligence that courts have distinguished from "active negligence."

Because Rhode Island General Laws § 27-8-15 immunizes insurance companies from claims relating to inspections conducted in connection with the issuance of insurance policies, including casualty policies, the Court should dismiss the Plaintiffs' complaint as to Essex Insurance Company.

II. Public Policy Dictates That This Court Not Expand Rhode Island Law To Recognize a Tort of Negligent Insurance Inspection.

Rhode Island has determined as a matter of public policy that an inspection conducted in connection with the issuance of and insurance policy, even if imperfectly performed should not subject an insurance company to liability. While the Court may, or may not, agree with such policy, it is bound to apply it. *See Cantwell v. University of Massachusetts*, 551 F.2d 879, 880 (1st Cir. 1977) ("Our duty is to interpret and apply state law as it now is."); *Gravina v. Brunswick Corp.*, 338 F. Supp. 1, 2 (D.R.I. 1972) ("It is well settled that a federal court sitting in a diversity action is bound to apply the applicable state law as the state court has declared it."). Even if the Court were to rule that Essex is not afforded statutory immunity in this case, it should decline to expand Rhode Island law to recognize a new tort of negligent insurance inspections. It is not the province of federal district courts to blaze new state common law trails. *See Carlton v. Worcester Ins. Co.*, 923 F.2d 1, 3 (1st Cir. 1991) (instructing that litigants in federal district courts "cannot expect new [state-law] trails will be blazed.") (brackets in original) (quotation and citation omitted); *Liu v. Striuli*, 36 F. Supp. 2d 452, 468 (D.R.I. 1999) (rejecting plaintiff's invitation to expand tort liability beyond parameters recognized by the Rhode Island Supreme Court); *Brainard v. Imperial Manufacturing Co.*, 571 F. Supp. 37, 40 (D.R.I. 1983) (instructing that a plaintiff litigating in federal court "is in a particularly poor position to assert a common law cause of action not previously recognized by the state courts.").

The utility of insurance inspections cannot be seriously challenged. As the Massachusetts Supreme Judicial Court has noted, its insurance inspection immunity statute "represents a legislative determination that an insurer is not to be penalized for making or not making a voluntary safety inspection for its own benefit and as an incident of its insurance business. That determination essentially expresses a policy determination analogous to that

expressed in *Matthews v. Liberty Mut. Ins. Co.*, 354 Mass. 470 (1968)." *Hamel v. Factory Mutual Eng'g Assoc.*, 409 Mass. 33, 36 (1990). In *Matthews*, the court explained that

> [I]nsurance companies which engage in accident prevention work, the social desirability of which cannot be questioned, should be able to do so without incurring unlimited liability for failing to discover a hazard that some jury might think ought to have been discovered. If an insurance company can escape tort liability altogether by not making any inspections on the premises of the insured, but may incur unlimited tort liability by making some inspections, it more than likely will decline to make any, unless required to do so by statute. The ultimate losers will be workmen and their families.

Matthews, 354 Mass. at 473.

The gravamen of the Plaintiffs' theory of liability against Essex is that Essex failed to guard or warn third parties (i.e., all patrons of The Station for all time) from any and all risks that some unspecified, all-encompassing inspection of the premises would have revealed. If this new theory of liability is accepted by the Court, it would alter the central tenets of the relationship between insureds and their insurers. This application of the Restatement would turn the role of insurer into a guarantor of the safety of anyone on the premises of an insured.

The Rhode Island Supreme Court has never ruled that an insurance company can be held liable to a third party for personal injury damages allegedly caused by an insurer's negligent inspection of an insured's premises. On the contrary, the Rhode Island Supreme Court has consistently held that insurers do not owe third parties a duty of good faith. That Court has observed that the "adversarial relationship between the claimant and the insurer, coupled with the fact that plaintiff was not a party to the contract, militates against the viability of any contractual claim of an alleged bad-faith action by defendant." *Cianci v. Nationwide Ins. Co.*, 659 A.2d 662, 667 (R.I. 1995).

Further, *Cianci* held that an injured party had no standing to bring an action for bad faith against an insurance company when said party was not the insured and was not a party to the

contract of insurance. The Court in *Cianci* relied on *Auclair v. Nationwide Mutual Ins. Co.*, 505 A.2d 431 (R.I.1986) (per curiam), for the proposition that the insurer of a third party is not liable to a claimant in an action for bad faith or breach of fiduciary relationship. *See Cianci*, 659 A.2d at 667. In *Auclair* the Court held that the relationship between a claimant and the insurer of an alleged tortfeasor was adversarial and that any obligation to deal in good faith ran only to the insured. *See Auclair*, 505 A.2d at 431. *See also Canavan v. Lovett, Schefrin & Harnett*, 745 A.2d 173 (R.I. 2000).

The Rhode Island Supreme Court has not recognized the viability of a claim for negligent insurance inspection under Restatement (Second) of Torts § 324A, and there is no indication that it would recognize such a claim. Section 324A provides that:

> One who undertakes, gratuitously or for consideration, to render services for another which he should recognize as necessary for the protection of a third person ..., is subject to liability to the third person for physical harm resulting from his failure to exercise reasonable care to perform his undertaking if:
>
> (a) his failure to exercise reasonable care increases the risk of such harm, or
>
> (b) he has undertaken to perform a duty owed by the other to the third person, or
>
> (c) the harm is suffered because of the reliance of the other or the third person upon the undertaking.

Restatement (Second) of Torts § 324A.

This Court recently declined to recognize a cause of action analogous to § 324A in the absence of clear authority that Rhode Island Supreme Court would do so. In *Travelers Ins. Co. v. Priority Business Forms, Inc.*, 11 F. Supp. 2d 194 (D.R.I. 1998), this Court observed that it is "not at all clear that the theory of § 323 (a similar Restatement provision regarding liability to first parties, as opposed to third parties, for negligently undertakings to render services) has been adopted in Rhode Island." *Id.* at 202. This Court in *Traveler* noted the absence of Rhode Island Supreme Court authority supporting the abandonment of traditional rules of proximate causes

and expressed "serious doubt that such a case is forthcoming." *Id.* Thus, this Court in *Travelers* exhibited a well-founded reluctance to expand Rhode Island common law beyond its established parameters. The same reluctance should be exercised here to reject plaintiffs' attempt to impose liability on Essex under § 324A in the absence of clear guidance from the Rhode Island Supreme Court.

Plaintiffs' argument that *Buszta v. Souther*, 102 R.I. 609, 232 A.2d 396 (1967), signaled the wholesale adoption of § 324A in Rhode Island is unavailing. *Buszta* did not involve an attempt to establish liability against an insurer for negligent inspection of premises. Rather, the case addressed whether an automobile inspector could be held liable for negligently inspecting a car, which negligence results in injuries to a third party. Under the particular circumstances of the case, the Court held that Rhode Island law would recognize such a claim, noting that allowing liability under such circumstances was "in accord with the modern view as expressed in the Restatement, Torts 2d, §324A." Key to the Court's decision in *Buszta* were important facts and considerations not present here. The inspections in *Buszta* involved dangerous instrumentalities that the General Assembly has mandated be inspected to "promote highway safety and reduce the shocking repeated instances of injuries, death and property damage which have been attributable to malfunctioning and improperly equipped motor vehicles." 102 R.I. at 615. Moreover, state law requires, *inter alia*, that inspectors acquire permits, perform certain designated safety checks, and issue official certificates of inspection and approval. *See id.* at 611, n.1. Thus, automobile inspections are an important part of a comprehensive state-mandated and state-regulated program implemented for public safety purposes. Under these unique circumstances, public policy dictates that a third party injured as a result of a negligent automobile inspection be allowed to pursue a cause of action against the inspector.

These considerations are not present in the case where a casualty insurance company inspects commercial premises. Such inspections are not mandated by law, are not required to be performed in a specific manner or encompass specific checks, are not required to result in the issuance of an official certificate of approval, and do not involve the inspection of dangerous instrumentalities. Moreover, declining to permit an insurance company to incur liability in tort for a negligent inspection of premises would not "serve [] to frustrate [an] obvious legislative intent" to protect the public from harm. *Id.* at 616. *Buszta* is limited to its facts and cannot reasonably be construed as authority for permitting a cause of action against Essex under § 324A of the Restatement under the facts of this case. Indeed nothing in Rhode Island Supreme Court precedent which would indicate the Court would adopt § 324A to allow an insurance company to be held liable to a third party for the negligent inspection of a client's commercial premises.

Further highlighting the lack of viability of the Plaintiffs' claims against Essex is the case of *McAleer v. Smith*, 791 F. Supp. 923 (D.R.I. 1994). In *McAleer*, this Court considered a claim involving the alleged negligent inspection of a seagoing vessel, the S/V MARQUES, by an insurance underwriter, the Yachtsman Syndicate ("Yachtsman"), an agent of Lloyds of London ("Lloyds"). Following this inspection, the vessel sank in high seas. Nineteen persons drowned, including a sixteen-month old infant. This Court granted summary judgment to Lloyds on the Plaintiffs' "negligent inspection" claim, ruling that "Yachtsman's alleged failure to properly inspect the vessel did not amount to a breach of duty that ran to plaintiffs or their decedents." 791 F. Supp. at 934-35. Although it acknowledged the tragic circumstances involved in the case, the Court rightly resisted plaintiffs' attempt to exploit that tragedy by imposing on insurers a new, overarching theory of third-party liability.

As part of their underwriting and loss control activities, many commercial property and casualty writers inspect insured locations and operations. Inspections usually are relatively quick, simple, and cursory surveys by lay inspectors (e.g. , checking for the presence of an automatic sprinkler system, unsafe storage of flammable liquids or chemicals, obvious tripping hazards, etc.). After performing the inspection, an inspector prepares a written report for the insurer, which may or may not include suggested recommendations for how the insured can reduce its loss experience, and therefore the profitability of the insurer's business. Generally, copies of inspection reports are provided to the policyholder, so it may consider and perhaps act on the inspector's suggested recommendations.

Such inspections (a) assist the underwriter to evaluate the hazards for which the insurer could be liable under its policy, (b) help the insurer formulate recommendations that, if accepted and acted upon by the insured, are believed likely to improve the insured's loss experience, and therefore the insurer's profit from the business, and (c) update the insurer's general background information about insured locations and operations for its own internal research purposes. The inspector's activities are directed to those ends, and not to advising the insured generally on matters affecting the safety of its employees or invitees. If an underwriting or loss prevention inspection results in improved personal safety it is merely an incidental by-product of the inspection's actual purpose of improving the profitability of the insurer's business. The inspection function is therefore regarded by insurers as essentially self-serving, performed for an insurer's own benefit, and not for the benefit of either policyholders or third parties. In recognition of the self-serving nature of such inspections, policies typically contain a provision disclaiming the insurer's obligation to inspect the insured's property and disclaiming any

warranty of the conclusions of such an inspection. The Essex policy issued to The Station nightclub contained such a provision in the section dealing with inspections and surveys:

> D. Inspections and Surveys
>
> We have the right but are not obligated to:
>
> 1. Make inspections and surveys any time
> 2. Give you reports on the conditions we find; and
> 3. Recommend changes.
>
> Any inspections, surveys, reports or recommendations relate only to insurability and the premiums to be charged. We do not make safety inspections. We do not undertake to perform the duty of any person or organization to provide for the health or safety of workers or the public.
>
> And we do not warrant that conditions:
>
> 1. Are safe or healthful; or
> 2. Comply with laws, regulations, codes or standards.
>
> This condition applies not only to us, but also to any rating, advisory rate service or similar organization which makes insurance inspections, surveys, reports or recommendations.

Common Policy Conditions, §D.

This language clearly demonstrates that any insurance inspection Essex performed was for the benefit of Essex's underwriters, and was not for the benefit of its insured or for any other third parties, including these Plaintiffs.

The Plaintiffs claim that Essex, by inspecting The Station nightclub, incurred a duty to The Station, its employees, and even members of the general public at The Station. The nature of that claimed duty is to identify and bring to the insured's attention – and perhaps to the attention of others – all identifiable conditions posing a risk of personal injury. In attempting to reduce their claims to that simplistic formula, Plaintiffs have ignored a major threshold requirement to the applicability of § 324A: that the insurer have undertaken to render services to

another, which the insurer should recognize as necessary for the protection of a third party or his things. "Undertaking" means an actual assumption of responsibility to perform a service principally for the benefit of another. *See James v. State*, 457 N.Y.S.2d 148 (N.Y. App. Div. 1982), *aff'd*, 457 N.E.2d 802 (N.Y. 1983). The *James* court noted that the rules that one who assumes to act may thereby become subject to the duty to act carefully "[h]as been limited [] to apply only to those situations wherein the action taken is for the benefit of another and not in furtherance of the interest of the one who assumes to act." 457 N.Y.S.2d at 150.

As clearly stated in the policy language, the inspection of The Station nightclub's premises and operations conducted by Essex in this case was conducted for the insurer's own benefit, as part of its routine underwriting and loss prevention practices, and did not constitute an undertaking to render services to another. *See, e.g., Jansen v. Fidelity & Cas. Co. of New York*, 566 N.Y.S.2d 962, 964 (N.Y. App. Div. 1991), *aff'd*, 589 N.E.2d 379 (N.Y. 1992); *Smith v. Allendale Mutual Ins. Co.*, 303 N.W.2d 702 (Mich. 1981); *Riverbay Corp. v. Allendale Mut. Ins. Co.*, 1988 WL 52783 (S.D.N.Y. 1988); *Leroy v. Hartford Steam Boiler Insp. & Ins. Co.* , 695 F. Supp 1120, 1126 (D. Kan. 1988) (general liability insurer which inspected insured's plant for its own loss prevention and underwriting purposes was not liable to insured's employees for its alleged negligent failure to discover safety hazard at plant). Courts have held that explicit policy language (permitting, but not requiring, the insurer to inspect for its own benefit) controls over any marketing documents that might suggest an intent to benefit the insured. *See, e.g., James,* 457 N.Y.S.2d at 151 ("We cannot read the express language out of the contract in order to convert this inspection, conducted for defendant's own benefit, into an inspection for the benefit of third parties.").

Considerations of fairness and public policy provide strong reasons for not imposing liability on insurers absent a clear § 324A undertaking. The reasons of fairness were cogently stated almost thirty years in *Nelson v. Union Wire Rope Corp.*, 199 N.E.2d 769 (Ill. 1964):

> The result is that an insurer who makes supplemental inspections, designed to minimize potential losses by diminishing the likelihood of injury, is penalized by the imposition of full responsibility for all losses that might have been revealed by the most complete inspection, even though no one concerned relied upon the insurance company for a complete inspection.

Id. at 796 (Schaefer, J., concurring in part and dissenting in part).

Imposing indiscriminate liability on insurers will either discourage insurers from performing some inspections (eventually leading to inaccurate pricing and some otherwise avoidable losses), or lead insurers to have more costly inspection programs than necessary for their own purposes, and to pass on those added costs (plus the costs of settlements, judgments, and Errors and Omissions coverage, if available) to their insureds. Premiums would have to be increased to account for this new, unintended public liability exposure.

Finally, the law should not unnecessarily discourage insurers from making these limited inspections for their own underwriting and loss prevention purposes, because even imperfect inspections will detect and cure far more hazards than they miss, and are better than none at all.

The practical consequences of adopting the rule advanced by Plaintiffs should also cause concern. Assuming that a duty to conduct a full-blown inspection exists, what would that duty require an insurer to do once it has discovered all discoverable hazards? More than to notify the insured of their existence? If the insured rejects or ignores the insurer's recommendations would the insurer then be obligated to communicate its observations directly to the insured's employees, invitees, and customers? Such actions by the insurer could invite litigation for defamation, bad

faith, interference with contractual relations, and other claims. Plaintiffs' lawyers are essentially arguing an insurer has an overriding duty to communicate the information to the world at large.

The subject of virtually every insurance policy is inspected prior to the issuance of a binding insurance policy. The purpose of the inspection is to assist the insurer's underwriters to determine whether to accept the risk of writing the policy and, if so, what a proper premium for the insurance should be. The purpose of the inspection is not to assist the insured in reducing its own risks or to warn the public about risks to the insured's premises. The insurance inspection is not a comprehensive industrial survey. Because different companies may be willing to accept more or less risk, or more or less risk at a particular point in time, there can never be one standard for a proper pre-insurance inspection. A "reasonably prudent" insurance inspection is whatever the individual insurance company wants it to be for its own purposes. The plaintiffs seem to argue that an insurance inspection that satisfies the insurance company's underwriting requirements is not enough. If not, then what is? An inspection that lists in detail every defect and deficiency that exists on an insured's premises? What if the insured does not repair the deficiency? Is the insurer liable if it does not report it to the proper authorities? Is the insurer liable for all time and to all persons for a missed defect? What if a life insurance company examination fails to detect a physical disease in one of its insureds? Will it be liable for negligently conducting the physical? Insurers could be exposed to limitless liability and would never be able to accurately assess risks in order to establish rational premiums. The result would be a reduction or elimination of insurance coverage. After The Station nightclub fire, Rhode Island does not need another disaster.

As the court in *Kotarski v. Aetna Cas. & Surety Co.*, 244 F. Supp. 547, 558 (D. Mich. 1965), correctly observed:

> If insurers are to be held liable in tort ... every time such an inspection fails to reveal a preventable accident, it would be in effect strict liability. Such additional liability should be imposed only by the legislature and not by the court.

Recognition of a viable cause of action against Essex in this case would change Essex from an insurer into a guarantor, without limits, of the safety of the safety of every invitee of every one of its insureds, whose premises it chooses to inspect for its own benefit. This vast expansion of liability should be only be determined by the Rhode Island General Assembly..

CONCLUSION

Rhode Island General Laws § 27-8-15 immunizes insurance companies from claims relating to inspections conducted in connection with the issuance of insurance policies, including casualty policies. Essex Insurance Company issued a policy of general liability insurance to the owners of The Station nightclub. A general liability insurance policy is a specie of casualty insurance policy. Essex did not create the condition that was the proximate cause of the personal injuries, death and loss described in the Plaintiffs' complaint. The Court should dismiss the Plaintiffs' complaint as to Essex Insurance Company.

It would take a great leap for this Court to rule that a cause of action exists in Rhode Island for the alleged tort of negligent insurance inspection. Rhode Island as a matter of law and policy has determined that so-called negligent insurance inspections will not lead to the imposition of liability on insurance carriers. Moreover, the Supreme Court of Rhode Island has not ventured to extend such liability to insurance carriers, and under the prior rulings regarding Restatement (Second) of Torts § 342A, probably never will. Any expansion of such liability involves important public policy consideration that should be determined by the Rhode Island legislature.

PCI sympathizes with the victims and the families of those who lost their lives in the terrible conflagration at The Station. However, these difficult, unsettling and emotionally charged facts should not make bad law. For the reasons set forth above, PCI respectfully requests that the Court dismiss Plaintiffs' claims against Essex.

Respectfully submitted,

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CERTIFICATION

I certify that on 16th day of November, 2004, I served a true copy of the within document via first class mail, postage prepaid to the parties listed below.

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